AUDIT DIVISION STATISTICAL STUDY

The Audit Division Statistical Study addresses the requirements set forth by IC 6-8.1-14-4 (2). The information is based on 100 percent of the audits completed, taxpayers assisted and special projects conducted during Fiscal Year 2005.

See Page 16 for an index of exhibits and charts included.

Taxpayers Served in District Offices

Taxpayer assistance is available in all district offices. Each office has a taxpayer assistance supervisor and assistant taxpayer assistance supervisor who perform taxpayer service functions, as well as other office support responsibilities. Each office has at least one field investigator who supports taxpayer assistance and performs collection functions in the district. Contract employees are available throughout the year to support taxpayer assistance.

The "Taxpayer Assistance Report-Fiscal Year 2005" (Exhibit A) provides the number of taxpayers assisted (in person and by telephone) and the amount of money collected and assessed at each office by the taxpayer assistance program. Exhibit A reveals that during Fiscal Year 2005, district offices assisted 130,103 taxpayers in person and 151,122 taxpayers through telephone contact. Total number of taxpayers served by the district offices were 281,225. The district office in Fort Wayne served 20,397 taxpayers in person, the highest number of any district office. The Columbus District Office served 18,378 taxpayers in person, the second highest total.

The Fort Wayne District Office served 23,859 taxpayers by telephone, while the Merrillville District Office served 20,928 taxpayers by telephone. This was the highest number of telephone contacts among the district offices, totaling 30 percent of total taxpayer telephone contacts. The Fort Wayne District Office served a total of 44,256 taxpayers by telephone and walk-in assistance, while Clarksville served 36,309 taxpayers by telephone and walk-in assistance.

"Field Auditors Taxpayer Assistance/Special Project Statistics" (Exhibit B) provides the number of hours devoted by field auditors in the district offices to assisting taxpayers and conducting special projects. The exhibit reveals that 8,527 auditor hours were channeled in this direction.

Gross Income Tax Violations

The most frequently violated gross income tax rule in the 2005 study was 45 IAC 1.1-2-4. Rule 2-4 defines taxable high rate income of utilities, display advertising, sale of real estate, rentals and extension of credit. This rule accounted for 21 (13.91 percent) violations of gross income tax rules in the 2005 study. Rule 45 IAC 1.1-2-4 and Rule 45 IAC 1.1-2-5 were equally rated in the 2004 report, with each Rule accounting for 26 (14.69 percent) of the violations. Rule 2-4 had been the most violated rule in the 2003 report with 16.78 percent of violations.

Ranking second in gross income tax violations was 45 IAC 1.1-2-2. Rule 2-2 defines taxable low rate gross income of retail and wholesale sales, display advertising, dry cleaning and laundry service, rental of water softening equipment, rental of rooms, lodging, booths and similar accommodations and commercial printing. Violations (18) of Rule 2.2 accounted for 11.92 percent of all violations of the gross income tax rules in the 2005 statistics. Rule 2-2 and Rule 3-3 tied for second in violations in the 2004 report with each Rule, accounting for 11.30 percent of violations. Rule 2-5 had been the second most violated gross income tax rule in the 2003 study with statistics showing 43 (14.73 percent) infractions.

Ranking third with 16 (10.60 percent) infractions of the gross income tax rule violations was Rule 45 IAC 1.1-2-1. This rule defines Indiana source income. Rule 2-1 was the third most frequently violated rule in 2004 (5.08 percent). Rule 2-2 (defined above) ranked third in the 2003 study with 37 (12.67 percent) violations.

Sales/Use Tax Violations

The most frequently violated sales and use tax rule was 45 IAC 2.2-3-20. Rule 3-20 states that if the seller of tangible personal property for storage, use or consumption in Indiana fails to collect the appropriate tax, the purchaser of such property must remit tax directly to the Department. This rule produced 550 violations (16.71 percent) of the sales and use tax infractions. In the 2004 study, Rule 3-20 accounted for 12.28 percent of sales and use tax infractions and ranked first. This rule had also ranked first in the 2003 study, accounting for 14.67 percent of sales and use tax violations. In the 2002 study, Rule 3-20 ranked first and accounted for 12.72 percent of sales and use tax infractions.

The second most frequently violated sales and use tax rule was 45 IAC 2.2-3-4. Rule 3-4 imposes use tax on “tangible personal property, purchased in Indiana or elsewhere in a retail transaction and stored, used or otherwise consumed in Indiana…unless the Indiana state gross retail tax (sales tax) has been collected at the point of purchase.” This rule accounted for 383 infractions or 11.64 percent of sales and use tax statute violations. Rule 3-4 ranked second in the 2004 study with 239 infractions (11.38 percent). The second most violated sales and use rule in 2003 was 45 IAC 2.2-3-4 (10.18 percent). Rule 5-8 (defined below) had been the second most violated rule in the 2002 study, accounting for 535 (11.25 percent) violations.

The third most violated rule for the 2005 fiscal year was 45 IAC 2.2-5-8. Rule 5-8 clarifies sales and use tax by providing examples of taxable and nontaxable sales of manufacturing machinery, tools and equipment used in direct production and other activities. Failure of taxpayers to comply with this rule accounted for 308 or 9.36 percent of the sales and use tax infractions. Rule 5-8 ranked third in the 2004 and 2003 studies with 195 (9.29 percent) and 363 (9.77 percent) infractions, respectively. Rule 3-4 had ranked third in the 2002 study with 518 (10.89 percent) violations.

Corporate Adjusted Gross Income Tax Violations

Corporate taxpayers violated adjusted gross income Rule 45 IAC 3.1-1-2 more than any other rule. This rule defines gross income for Indiana residents filing individual returns as all income defined by Section 61 of the Internal Revenue Code. Violations (64) of this rule accounted for 15.27 percent of the total violations in the 2005 study. Rule 1-8 (defined below) had been the most violated rule in 2004, 2003 and 2002 studies with 40 (15.81 percent), 76 (14.10 percent) and 94 (12.21 percent) infractions, respectively.

Rule 45 IAC 3.1-1-1 was the second most frequently violated rule under this study. This rule defines adjusted gross income as noted in Internal Revenue Code Section 62. These violations (58) accounted for 13.84 percent of the total violations for 2005. Rule 1-1 did not appear in the top three violated rules in the 2004 study. Rule 1-1 had ranked second in the 2003 study with 63 violations, accounting for 11.69 percent of infractions. Ranking second in the 2004 report was 45 IAC 3.1-1-9 (net operating loss deduction) with 10.67 percent of violations. Rule 1-9 had ranked second in the 2002 study with 79 (10.26 percent) violations.

The third most frequently violated adjusted gross income rule was 45 IAC 3.1-1-8. Rule 1-8 states that taxable income as defined in the Internal Revenue Code is modified in several ways to arrive at Indiana adjusted gross income. Violations (54) of this rule accounted for 12.89 percent of the violations of adjusted gross income tax rules. The 2004 and 2002 studies revealed 45 IAC 3.1-1-97 ranked third with 26 (10.28 percent) and 72 (9.35 percent) of the violations, respectively. The third most violated rule in the 2003 study was 45 IAC 3.1-1-9, accounting for 61 (11.32 percent) infractions.

Dollar Amounts of Tax Assessed

Exhibits C, D and E display the amount of assessments (refunds) of the gross income tax, sales tax and adjusted gross income tax administrative rules, respectively. “Total assessments” for any tax type represent gross assessments less amounts refunded.

The amount assessed or refunded for each of the most frequent violations and the percentage of the amount to total net assessments are presented below:

Gross Income Tax—Exhibit C:

	Amount Assessed	Percentage of All Assessments
45 IAC 1.1-2-4	$1,714,988	10.41%
45 IAC 1.1-2-2	$ 16,971	.11%
45 IAC 1.1-2-1	$1,201,391	7.29%

Sales/Use Tax—Exhibit D:

	Amount Assessed	Percentage of All Assessments
45 IAC 2.2-3-20	$3,085,671	18.17%
45 IAC 2.2-3-4	$1,771,875	10.44%
45 IAC 2.2-5-8	$ 986,290	5.81%

Corporate Adjusted Gross Income Tax—Exhibit E:

	Amount Assessed	Percentage of All Assessments
45 IAC 3.1-1-2	$ 162,234	.66%
45 IAC 3.1-1-1	$ 497,422	2.03%
45 IAC 3.1-1-8	$6,738,981	27.49%

Industry/Business Most Frequently in Violation

Gross Income Tax

Taxpayers engaged in information, publishing, telecommunications, finance, rental, insurance, real estate, leasing and professional services most frequently violated the gross income tax rules. This group committed 44 violations or 29.14 percent of the total violations. The gross income tax rules most frequently violated by this group of taxpayers are 45 IAC 1.1-2-1 and 45 IAC 1.1-2-4 (seven violations each). Rule 2-1 defines "Indiana source income," while Rule 2-4 defines "high rate income."

The second largest number of gross income tax violations was committed by taxpayers in the manufacturing business. This group committed 41 infractions, or 27.15 percent of the total violations for 2005. The most frequently violated rule of this group was 45 IAC 1.1-3-3, which defines exempt gross income derived from business conducted in interstate commerce. The manufacturing business had ranked first in infractions for the previous twelve years.

Sales and Use Tax

For the 2005 reporting period repair, personal and other service businesses accounted for the most infractions. They accounted for 713 violations, or 21.67 percent of the total sales and use tax violations. The most frequently violated rule by these taxpayers was 45 IAC 2.2-3-20 that states if a seller of tangible personal property for storage, use or consumption in Indiana fails to collect the appropriate tax, the purchaser of such property must remit tax directly to the Department.

Manufacturing businesses had the second most frequency of violations for the sales and use tax rules. There were 586 violations committed by this group, representing 17.81 percent of the total violations. The rule most frequently violated by this group was 45 IAC 2.2-5-8, which clarifies sales and use tax by providing examples of taxable and nontaxable sales of manufacturing machinery, tools and equipment used in direct production and other activities.

Adjusted Gross Income Tax

Repair, personal service and other service providers with 164 infractions were the most frequent violators of adjusted gross income tax rules. This figure represents 39.14 percent of the total adjusted gross income tax violations. Adjusted gross income for individuals, defined by 45 IAC 3.1-1-2, accounted for the most infractions in this class.

Manufacturing businesses ranked second in violation of the adjusted gross income rules. They committed 57 infractions, or 13.60 percent of the adjusted gross income tax violations. Rule 1-8 (45 IAC 3.1-1-8), which discusses modifications of federal adjusted gross income in determining Indiana adjusted gross income, was the most violated rule by this industry group.

Special Tax Violations

Exhibit G provides the special tax assessments and refunds by citation.

Article VIII (citation R800 on exhibit) of the International Fuel Tax Agreement (IFTA) was the most frequently violated special tax item in the study. It specifies the taxable event is the consumption of motor fuels in the propulsion of qualified motor vehicles, except fuel consumed that is exempt from taxation by a jurisdiction. All motor fuel acquired that is normally subject to consumption tax is taxable, unless proof to the contrary is provided by the licensee. Article VIII was violated 235 times and yielded $327,854 in net assessments for the State of Indiana. This represents 23.74 percent of total violations and 6.12 percent of net assessments.

Article X (citation R1000 on exhibit) of the International Fuel Tax Agreement (IFTA) was the second most frequently violated section of the special tax statutes. This Article discusses how taxpayers can obtain credit for tax previously paid on purchases of fuel at the pump. It also lists the records needed to substantiate the refund request. This article was violated 221 times, accounting for 22.32 percent of the total violations. These violations resulted in net assessments of $162,948.

The taxpayer group most frequently in violation of the special tax statutes and IFTA Articles was the repair, personal and other service industries. This group committed 432 violations, accounting for 43.64 percent of the total infractions. Article VIII of the International Fuel Tax Agreement was most frequently violated by the repair, personal and other service industries.

Miscellaneous Code Violations

Exhibit F provides the assessment amounts for the following:

- Financial Institutions Tax
- Tax Administration
- Food and Beverage Tax
- Innkeeper's Tax
- Charity Gaming

A review of the Miscellaneous Code violations data reveals that 45 IAC 15-9-2 was the most frequently violated Rule with 12 (14.63 percent) infractions in the Fiscal Year 2005 study. These violations yielded $205,125 in net assessments. Rule 9-2 discusses the statute of limitations for refunds. In the 2004 study, IC 6-8.1-4-2 (which discusses examination of records) produced 16 (12.12 percent) infractions. IC 6-8.1-9-1 was the most violated rule in the 2003 study with 57 (18.45 percent). IC 6-8.1-4-2 was the most violated rule in the 2002 study, accounting for 24 (14.46 percent) infractions.

The nine violations of 45 IAC 15-4-1 was the second most violated rule in this category in 2005. It yielded a total of ($47,384) in net refunds. Rule 4-1 defines access to taxpayer records. Nine rule violations accounted for 10.98 percent of the total infractions in this category.

Number of Years in the Audit Period

The audit period consistently averages three years.

Use of Professional Tax Preparation Assistance

The services of professional preparers were used in 75 percent of the corporate income tax returns and 11 percent of the sales tax returns. Statistics show that 26 percent of individuals use a professional preparer to complete the returns.

Filing of Appropriate Tax Returns

Rule 45 IAC 3.1-1-92 (Exhibit E) requires qualifying corporations to make estimated tax payments. Taxpayers in violation of this rule either failed to file estimated income tax returns or failed to remit the appropriate amount of tax. For the fiscal years ending in 2004 and 2005, no infractions were found. The 2003 study indicated eight violations of this rule, resulting in assessments in the amount of $12,863 and refunds totaling ($110,617).

Indiana Code 6-8.1-10-2.1 (Exhibit F) revealed no violations during the 2005 study period. This section specifies the penalty to be imposed if a taxpayer fails to file an appropriate return or pay the full amount of tax due. Violations of this section in the 2004, 2003 and 2002 studies were also zero.